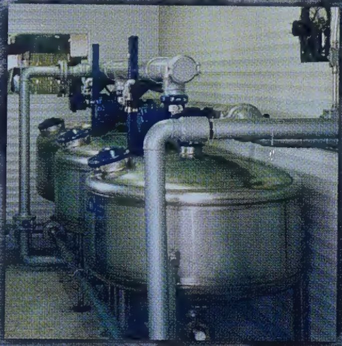
Baden
TECHNOLOGIES INC.



Annual Report 2002

www.baden.ca

Corporate Profile

Baden Technologies Inc. is a public company trading on the TSX Venture Exchange. Through its subsidiary FSI International Services Ltd. ("FSI"), Baden's core business is the development, marketing, manufacture, production, and installation of filtration and filtration-related products for the petrochemical, power generation, pulp & paper, and environmental industries.

FSI is a Calgary-based manufacturing and service company specializing in filtration and filtration-related technologies. Its primary market offerings are in the domestic oil and gas-related industries, and include:

- Filter Bags and Filter Vessels,
- Mobile Field Filtration Services,
- Portable Ultra Filtration Systems,
- MOLE Drill Cuttings Treatment Systems,
- AquaShield Water Removal Filters,
- Carbon Filtration Vessels,
- Telescoping Centrifuge Stands

FSI currently markets its product group in Canada and in international markets such as Russia and the Middle East. FSI has been operating in these industries since 1987.

FSI is also a global leader in the development, manufacture and installation of customized equipment in the Russian oil industry. FSI's Brine Blending Plant is a unique product, and demand for this specialized system from the major Russian oil companies is steadily increasing.

FSI is Baden's only subsidiary and is wholly owned by the Company.

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Financial Highlights

Years ended December 31	2002	2001
Revenue	$1,269,657	$ 9,891,718
Earnings		
Earnings Per Share [1]	(0.056)	0.087
Earnings Before Interest, Taxes, Depreciation & Amortization (EBITDA)	(753,238)	1,287,387
Cashflow from Continuing Operations		
Cashflow Per Share from Continuing Operations [1]	(0.048)	0.098
Working Capital		
Working Capital	1,353,606	865,035
Working Capital Per Share [1]	0.135	0.103
Net Book Value Per Share	0.186	0.139
Outstanding Shares		
Weighted Average	10,015,405	8,252,102
Weighted Average (fully diluted)	10,015,405	8,403,793
At Period End	13,056,501	8,816,501

[1] Per share figures, unless otherwise specified, are based on fully diluted share figures

Letter to Shareholders

Dear Fellow Shareholders:

Looking back on our previous annual report and my message to shareholders, I discussed the severe consequences from 9/11 domestically and internationally. The reduced capital expenditures that were immediately evident following this disaster had a prolonged effect on our business, most specifically in our primary market, Russia.

While we maintained cautious optimism for a business recovery from the fourth quarter of 2001 throughout 2002, it unfortunately became evident that the ramifications of this tragic event would last longer than we had hoped. Needless to say, we maintained a marketing push during the course of 2002, as our clients reassured us that all projects which were previously in active negotiations, were delayed and not cancelled.

Baden has always maintained a focused and lean organizational structure. We have a very low employee count and virtually no long term debt. This served us well throughout 2002, as it was our domestic operations which provided the majority of revenue. I am quite pleased to report that we only lost $563,000 on an 87% decrease in revenue. We hold a cash position of approximately $700,000 and our current assets exceed current liabilities by a factor of almost nine. We are in strong financial position.

Baden, through its wholly owned subsidiary, FSI International Services Ltd., has always received the vast majority of its business from large internationally-based oil and gas operators. As we continually recognize, this is at times a volatile marketplace which is often difficult to operate within, and even more difficult to forecast. Witness the unforeseen world-wide implications of a "non-energy" event which occurred so far away from our primary market. However, with volatility comes the expectation of higher reward.

As 2002 progressed, management began to evaluate the longer-term direction for the Company. Recognizing the perceived and real difficulties in focusing upon one market for the majority of revenues caused us to evaluate the means to diversify our revenue stream. Quite simply, we knew we had to broaden our international markets and intensify our efforts here at home.

In Canada we increased revenue by 10% on the strength of successful marketing of our inaugural Ultra Filtration System. This mobile system is used for the conditioning of turbine engine lubricants and large-scale hydraulic oil systems. Since the commissioning of the inaugural unit in August, the Ultra Filtration System has been utilized in a variety of oil/lubricant conditioning applications. I expect that we will expand our equipment base this year as the benefits of this system are becoming more evident in the power generation and energy sectors.

Subsequent to the end of the third quarter, Baden raised $676,000 by way of private placement via the issuance of 2,600,000 common shares at $0.26 per share. These funds will continue to assist

Baden in further developing its international markets, and financing the expansion of our Canadian operations. Funds were raised from an investor who is providing strategic guidance in identifying and arranging new business opportunities outside of our traditional marketplaces.

For a number of months in 2002, our Russian clients indicated that their capital spending budgets were to be strengthened for the 2003 fiscal year. In the first quarter of 2003, we signed a contract with Yukos Oil Company for the design, fabrication, installation and commissioning of a brine blending plant. The value was approximately $1.5 million CAD, and was the fourteenth plant constructed for sale internationally. This was our first significant sale since late 2001. Comparatively, the first contract for 2003 has exceeded results for all of 2002.

We expect confirmation for a variety of international endeavors over the coming months, including additional brine plant contracts, water filtration projects and other manufacturing contracts. As our expectation for further contracts materializes over the balance of 2003, our Russian business is again expected to provide the majority of revenue. Although large contracts will also dominate our business successes in 2003, the important difference is that we anticipate having a broader revenue stream than in prior years, including additional markets, products and services.

Over the years we have witnessed the ups and downs of the international energy equipment market. Business conditions have an ability to change rapidly and dramatically. At times we may experience a prolonged period of "stability". However, with the world currently experiencing a sustained level of relatively high commodity prices we believe that our business will perform well in 2003. Expectations provide a certain measure of reassurance in adverse conditions, but our unchanging attitude on how we conduct business, namely enforcing strong customer relationships and expansion for "the right reasons", provides proper perspective in adverse or positive conditions.

Again, I must express my sincere thanks to our shareholders and employees. The support of our employees and all of our stakeholders through a difficult year has been and is truly valued and appreciated.

On behalf of the Board of Directors

Richard Ball, President & CEO

Management's Discussion and Analysis

The following discussion is based on the Company's consolidated financial statements, which were prepared in accordance with generally accepted accounting principles. The discussion of financial conditions and results of operations should be read in conjunction with the consolidated financial statement and notes.

Overview

As was the case with the latter half of 2001, conditions in 2002 meant a significant downturn in the capital spending budgets of most domestic and Russian oil producers. It is upon these capital budgets that a large portion of Baden's revenue stream is reliant. The financial results for 2002 reflect decreased revenues internationally. Domestically, the Company enjoyed a slight increase in overall operating results.

Operating Results

During 2002, Baden experienced a significant decrease in revenue and earnings over 2001 results. Revenue for the year decreased to $1,269,657 from $9,891,718 (2001), a decrease of 87%. Net loss increased to $563,367 from net earnings of $728,127 (2001).

The decrease in earnings was primarily a result of the significant decrease in the sale of Brine Blending Plants and related equipment in the Russian market.

Cashflow and Earnings

Earnings before interest, taxes, depreciation and amortization (EBITDA) for the year decreased to a loss of $753,238 or $0.075 per share (EBITDA of $1,287,387 or $0.153 per share in 2001).

Net earnings decreased to a loss of $563,367 (or a loss of $0.056 per share) from earnings of $728,127 (or $0.087 per share in 2001). This represents a decrease in profitability of 177.4% for the year to year comparison.

Operating cashflow (excluding changes in non-cash working capital) decreased for the year ended December 31, 2002 to a net outflow of $484,490 from a net cashflow of $824,510 for the same period ended December 31, 2001. Cash increased $456,893 compared to a cash increase of $266,584 for the same period last year. Increased cash was a result of several private share placements that occurred throughout the year (see Note 9, Share Capital, below).

Operating Costs and Expenses

Selling, General and Administrative expenses ("SGA") increased to $800,439 from $673,059 in 2001, an increase of 18.9%. In years in which there are large contracts for items such as Brine Blending Plants, a portion of SGA is allocated to Cost of Sales.

Income Taxes

While the expected tax rate decreased to 39.24% (from 42.12% for 2001; combined Federal and Alberta income tax rates), the effective rates differed. The effective tax rate for 2001 was 38.42%. For 2002, there is a tax recovery resulting from the application of current year's losses to prior years' income.

Liquidity and Resources

Working capital for the year ended December 31, 2002 increased by 56.5% to $1,353,606 from $865,035 in 2001. This increase is due primarily to the cash provided by financing from the three private placements completed during the year.

The Company continues to be highly liquid., which is reflected in the increase in the current ratio (current assets divided by current liabilities) to 8.86 in 2002 from 2.83 in 2001. The majority of Baden's liabilities are in the form of current operating debts, and are significantly decreased ($172,159 at December 31, 2002 compared to $471,729 at December 31, 2001).

Despite decreased operational results, the Company continues to maintain good financial position through liquidity. This, in turn, means Baden is in good financial position for future project-specific borrowing requirements and expansion.

Risk and Uncertainty

The majority of the products provided by Baden are supplied to clients within the oil and gas industries, both in Canada and internationally. Many of these products are of sufficient size that they are included in the capital spending budgets of Baden's clients. These budgets are directly influenced by the world market price of oil, and for this reason, the purchase decisions of our clients are often beyond influence on the part of Baden's salespersons.

Also, the extended cycle of contract negotiation, production, and delivery of products such as the Brine Blending Plant mean that operating results may fluctuate significantly between financial reporting periods.

Baden maintains its commitment to its shareholders by maintaining operational efficiency and strong cost controls during periods of reduced market activity. The company also maintains a strong personal sales presence in its markets, both through our senior management team's client visits and through Baden's agents.

The Company also maintains public liability insurance, work-in-progress and inventory insurance, and foreign liability insurance. In all areas of our operations we attempt to protect both our shareholders and our valued employees.

In terms of mitigating payment risk from foreign clients, Baden (through its subsidiary FSI International) has developed a strong working relationship with the Canadian Commercial Corporation ("CCC"). CCC provides project-specific work-in-progress financing for many of FSI's foreign export contracts.

In over ten years of export sales, FSI has encountered no problems related to non-payment or bad debts on the part of our foreign clients.

Auditor's Report

To the Shareholders of Baden Technologies Inc.:

We have audited the consolidated balance sheet of Baden Technologies Inc. as at December 31, 2002 and 2001 and the consolidated statements of loss and retained earnings and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2002 and 2001 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Moody Shikaze Bartlett LLP

Chartered Accountants

Calgary, Alberta
March 14, 2003

Management's Report

The consolidated financial statements of Baden Technologies Inc. were prepared by management in accordance with accounting principles generally accepted in Canada. The financial and operating information presented in this statutory report is consistent with that shown in the financial statements.

Management has designed and maintains a system of internal controls to provide reasonable assurance that all assets are safeguarded and to facilitate the preparation of financial statements for reporting purposes. Timely release of the financial information necessitates the use of estimates when transactions affecting the current accounting period cannot be finalized until future periods. Such estimates are based on careful judgments made by management.

External auditors appointed by the shareholders have conducted an independent examination of the corporate and accounting records in order to express their opinion on the financial statements. The Audit Committee has met with the external auditors and management in order to determine if management has fulfilled its responsibilities in the preparation of the financial statements. The Audit Committee has reported its findings to the Board of Directors and the Board has approved the consolidated financial statements.

I. Richard Ball
President & CEO

Ian R. Ball
Chief Financial Officer

Audited Financial Statements

Consolidated Balance Sheets

December 31, 2002 and 2001

	2002 $	2001 $
ASSETS		
Current		
Cash	**698,177**	241,284
Accounts receivable	**378,593**	635,142
Inventories (Note 4)	**372,466**	399,125
Prepaid expenses and other	**76,529**	61,213
	1,525,765	1,336,764
Capital assets (Note 5)	**521,556**	346,738
Total Assets	**2,047,321**	1,683,502
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current		
Bank loan (Note 6)	-	60,000
Accounts payable and accrued liabilities	**152,868**	255,635
Deferred revenue	-	140,166
Current portion of long term debt (Note 7)	**19,291**	15,928
	172,159	471,729
Long term debt (Note 7)	**10,481**	31,373
Future income taxes (Note 8)	-	12,421
Total Liabilities	**182,640**	515,523
Shareholders' equity		
Share capital (Note 9)	**1,638,426**	378,357
Retained earnings	**226,255**	789,622
Total Shareholders' Equity	**1,864,681**	1,167,979
Total Liabilities and Shareholders' Equity	**2,047,321**	1,683,502

Approved on behalf of the Board

Director

Director

Audited Financial Statements

Consolidated Statement of Loss and Retained Earnings

For the Years Ended December 31, 2002 and 2001

	2002 $	2001 $
Revenue	**1,269,657**	9,891,718
Expenses		
Cost of sales	**1,222,456**	7,931,272
Selling, general and administrative	**800,439**	673,059
Interest on long term debt	**20,186**	23,565
Amortization	**91,298**	83,962
	2,134,379	8,711,858
Income (loss) before income taxes	**(864,722)**	1,179,860
Income taxes (recovered)		
Current	**(288,934)**	439,312
Future	**(12,421)**	12,421
	(301,355)	451,733
Net income (loss)	**(563,367)**	728,127
Retained earnings (deficit) - beginning of year	**789,622**	(494,944)
Preferred shares	**-**	650,000
Normal course issuer bid	**-**	(93,561)
Retained earnings (deficit) – end of year	**226,255**	789,622
Earnings per share (Note 9)		
Basic	**(0.056)**	0.088
Diluted	**(0.056)**	0.087

Audited Financial Statements

Consolidated Statement of Cash Flows

For the Years Ended December 31, 2002 and 2001

	2002 $	2001 $
Operating activities		
Net income	**(563,367)**	728,127
Items not affecting cash		
Amortization	**91,298**	83,962
Future income taxes	**(12,421)**	12,421
	(484,490)	824,510
Change in non-cash working capital (Note 13)	**(35,041)**	(337,013)
	(519,531)	487,497
Investing activities		
Purchase of capital assets	**(266,116)**	(134,315)
Financing activities		
Issuance of shares	**1,225,000**	404,110
Proceeds on exercise of options	**92,500**	12,500
Normal course issuer bids	**-**	(104,081)
Share issue costs	**(57,431)**	(27,833)
Repayment of long term debt	**(17,529)**	(371,294)
	1,242,540	(86,598)
Increase in cash flow	**456,893**	266,584
Cash (deficiency) - beginning of year	**241,284**	(25,300)
Cash - end of year	**698,177**	241,284

Supplemental information		
Interest paid	**12,599**	20,644
Income taxes paid (recovered)	**(254,063)**	608,821

Notes to Financial Statements

1. Description of operations

The Company develops, manufactures, produces, installs, sells and rents various product groups intended to satisfy the filtration needs of the petrochemical, power generation, pulp and paper and environmental industries. The Company currently markets its product group in Canada and in international markets such as Russia and the Middle East.

2. Business combination

On March 30, 2001, Baden acquired all of the issued and outstanding common shares of FSI International Services Ltd. ("FSI") by issuing 6,000,001 common shares of Baden for a net purchase price of $404,110. After giving effect to the transaction, the former shareholders of FSI held approximately 66.67% of the common shares of the Company such that control of Baden passed to the former shareholders of FSI. Accordingly, the acquisition has been accounted as a reverse takeover using the purchase method whereby FSI is deemed to be the acquirer of the assets and operations of Baden.

The fair value of the net assets of Baden at the time of the deemed acquisition:

Cash	431,244
Working capital	(27,134)
	404,110

The cost of the deemed acqusition was paid as follows:

6,000,001 common shares	461,284
Transaction costs	(57,174)
	404,110

3. Summary of significant accounting policies

Basis of presentation

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiary, FSI International Services Ltd. They include the assets, liabilities and operations of FSI since incorporation. The operations of Baden Technologies Inc. are included from March 30, 2001.

Inventories

Inventory of parts and materials are valued at the lower of cost and net realizable value. Costs are determined on a first-in, first-out basis.

3. Summary of significant accounting policies *(continued)*

Capital assets

Capital assets are recorded at cost less accumulated amortization. Amortization is based on the assets' estimated useful lives.

Filtration equipment	20%	declining balance method
Computer equipment	30%	declining balance method
Office equipment	20%	declining balance method
Automotive	30%	declining balance method
Portable building	10%	declining balance method
Leasehold improvements	3 years	straight-line method
Computer software	100%	declining balance method

Revenue recognition

Manufacturing revenues and product sales are recognized when the products are delivered to the customer.

Installation revenues are recognized on a percentage of completion basis throughout the installation phase of the contract.

Rental revenue is recognized when the equipment's service is provided.

Parts sales revenue is recognized when the goods are shipped.

Income taxes

Income taxes are recorded using the liability method of accounting. Under this method, future income tax liabilities are determined by applying the tax rate at the end of the accounting period to the temporary difference between the accounting and tax bases of the Company's assets and liabilities. The future benefit of current and past tax losses is recognized whenever it is more likely than not that the Company will be able to generate sufficient future taxable income to utilize the tax losses before they expire.

Earnings per share

Effective January 1, 2001, the Company adopted a new accounting standard relating to the calculation and disclosure of per share information. Under the new standard, diluted per share information is calculated using the treasury stock method. The treasury stock method assumes the notional exercise of all in-the-money stock options and that all notional proceeds to the Company are used to repurchase the Company's stock at the average market price during the period. No adjustment to diluted earnings per share is made if the result of this calculation is anti-dilutive.

3. Summary of significant accounting policies *(continued)*

Stock based compensation

The Company has a share option plan. No compensation expense is recognized when stock options are issued pursuant to the plan. Amounts received on exercise of stock options are credited to share capital.

Use of estimates

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reported period. The most significant of these estimates are related to the recording of inventory and capital assets. Actual results could differ from these estimates.

4. Inventories

	2002 $	2001 $
Parts and materials	**181,195**	211,090
Work in progress	**191,271**	188,035
	372,466	399,125

5. Capital assets

	2002		
	Cost	Accumulated amortization	**Net book value**
	$	$	**$**
Filtration equipment	625,061	251,386	**373,675**
Computer equipment	130,803	86,516	**44,287**
Office equipment	75,832	52,730	**23,102**
Automotive	107,517	56,197	**51,320**
Portable building	39,208	10,314	**28,894**
Leasehold improvements	16,011	15,733	**278**
Computer software	18,400	18,400	**-**
	1,012,832	491,276	**521,556**

	2001		
	Cost	Accumulated amortization	Net book value
	$	$	$
Filtration equipment	363,471	202,980	160,491
Computer equipment	126,277	68,386	57,891
Office equipment	75,832	48,177	27,655
Automotive	107,517	43,365	64,152
Portable building	39,208	7,105	32,103
Leasehold improvements	16,011	14,634	1,377
Computer software	18,400	15,331	3,069
	746,716	399,978	346,738

Capital assets include assets under finance contracts in the amount of $52,320.

6. Bank loan

The bank loan bore interest at prime plus 1.25%, was due on demand, and was supported by a general assignment of book debts, the limited personal guarantees of the President and his spouse, and an assignment of insurance on the life of the President. The effective interest rate as at December 31, 2001 was 5.25%. The maximum credit limit available was the lessor of $125,000 and 75% of accounts receivable.

In June 2002, the bank loan was repaid and the Company did not renew the credit facility.

7. Long term debt

	2002 $	2001 $
Finance contracts, repayable in monthly blended installments of $1,776 including principal and interest charged at 10.5% per annum, due between May 2004 and July 2004. The finance contracts are secured by the title to certain vehicles.	**29,772**	47,301
Current portion	**(19,291)**	(15,928)
	10,481	31,373

Principal repayment terms are approximately:

2003	17,529
2004	19,291
2005	10,551
	47,371

8. Income taxes

The components of the future income tax liability at December 31, 2002 and 2001 are as follows:

	2002 $	2001 $
Future income tax assets:		
Non-capital losses carried forward	**46,297**	-
Share issue costs	**71,884**	-
	118,181	-
Future income tax liabilities:		
Capital assets	**13,917**	12,421
Net future income tax asset before valuation allowance	**104,264**	(12,421)
Valuation allowance	**(104,264)**	-
Net future income tax liability	**-**	(12,421)

8. Income taxes *(continued)*

The provision for income taxes differs from the result which would be obtained by applying the combined Canadian federal and provincial statutory income tax rate of 39.24% to income before income taxes. The difference results from the following:

	2002	2001
	$	$
Income (loss) before provision for income taxes	**(864,722)**	1,179,860
Expected tax at 39.24% (2001 - 42.12%)	**(339,317)**	496,957
Realization of previously unrecognized loss carryforwards	**-**	(55,581)
Non-recognition of benefit of current year's tax loss	**44,181**	-
Other	**(6,219)**	10,357
Income tax expense (recovery)	**(301,355)**	451,733

The Company has $112,591 in non-capital losses available to claim against future taxable income which expire in 2009.

9. Share capital

Authorized share capital:

Unlimited common shares
Unlimited preferred shares

Issued:

	2002		2001	
	Number of shares	**Stated value $**	Number of shares	Stated value $
Common shares				
Balance, begining of year	**8,816,501**	**378,357**	3,000,000	100
Issued for cash	**3,900,000**	**1,225,000**	-	-
Issued in respect of reverse takeover	**-**	**-**	6,000,001	404,110
Acquired and to be cancelled	**-**	**-**	(233,500)	(10,520)
Issued on exercise of stock options	**340,000**	**92,500**	50,000	12,500
Share issue costs	**-**	**(57,431)**	-	(27,833)
	13,056,501	**1,638,426**	8,816,501	378,357

In November 2002, the Company issued 2,600,000 common shares at a price of $0.26 per share for total gross proceeds of $676,000 on a private placement issue. The cost

of issuance was $2,980.

9. Share capital *(continued)*

On June 26, 2002, the Subscriber sold 300,000 common shares to an unrelated third party for $0.43 per share for total gross proceeds of $129,000. The Company then issued 300,000 units to the Subscriber for aggregate proceeds of $129,000. The cost of issuance was $12,730. Each unit consists of one common share of the Company and one-half common share purchase warrant. Each common share purchase warrant entitles the holder to purchase one common share of the Company at any time on or before June 26, 2004 for $0.60. The warrants were issued to compensate the Subscriber for exchanging free trading shares for restricted shares and for triggering a taxable event. It is management's opinion that the warrants represent a cost of obtaining the $129,000. The estimated fair value of the warrants of $0.30 per share has been determined using the Black-Scholes option-pricing model on the assumption that the volatility is 132%, the expected life is 2 years, and the risk-free rate of return is 3.0%. The aggregate fair value of the warrants issued being $34,000 is equal to the fair value of the share issue costs and no adjustment is required to shareholders' equity.

On April 19, 2002, a private Alberta company wholly owned by a trust established for the benefit of the family of the president (the "Subscriber"), sold 1,000,000 common shares to an unrelated third party for $0.42 per share for total gross proceeds of $420,000. The Company then issued 1,000,000 units to the Subscriber for aggregate proceeds of $420,000. The cost of issuance was $41,721. Each unit consists of one common share of the Company and one-half common share purchase warrant. Each common share purchase warrant entitles the holder to purchase one common share of the Company at any time on or before April 19, 2004 for $0.50. The warrants were issued to compensate the Subscriber for exchanging free trading shares for restricted shares and for triggering a taxable event. It is management's opinion that the warrants represent a cost of obtaining the $420,000. The estimated fair value of the warrants of $0.34 per share has been determined using the Black-Scholes option-pricing model on the assumption that the volatility is 145%, the expected life is 2 years, and the risk-free rate of return is 3.0%. The aggregate fair value of the warrants issued being $140,000 is equal to the fair value of the share issue costs and no adjustment is required to shareholders' equity.

Stock options:

The Company maintains a Stock Option Plan (the "Plan") for directors and certain officers, employees and consultants of the company. Each option entitles the holder to acquire one share of the Company. The Board of Directors has reserved a total of ten percent (10%) of the issued and outstanding common shares of the Company for issuance of stock options. Stock options granted under the Plan may not be outstanding for a period of more than five years and the exercise price must be paid in full upon exercise of the option.

9. Share capital *(continued)*

A summary of the status of the Company's Plan and other options as of December 31, 2002, and changes during the period is presented below:

	2002		2001	
	Number of options	**Weighted average exercise price $**	Number of options	Weighted average exercise price $
Outstanding, beginning of year	**750,000**	**0.27**	500,000	0.25
Granted	**40,000**	**0.40**	300,000	0.30
Exercised	**(340,000)**	**0.27**	(50,000)	0.25
Outstanding, end of year	**450,000**	**0.28**	750,000	0.27
Exercisable, end of year	**420,000**	**0.27**	750,000	0.27

Options outstanding and exercisable:

	2002		2001	
Exercise price $	**Number outstanding**	**Weighted average remaining life in years**	Number outstanding	Weighted average remaining life in years
0.25	**260,000**	**2.70**	450,000	3.65
0.30	**150,000**	**3.25**	300,000	4.25
0.40	**40,000**	**4.67**	-	-
	450,000		750,000	

On September 1, 2002, 40,000 stock options were granted to a consultant of the Company. Each stock option entitles the holder to purchase one common share of the Company for $0.40. The stock options vest at a rate of 10,000 stock options per quarter, beginning December 1, 2002. The expiry date of the stock options is September 7, 2007.

Normal course issuer bids

Pursuant to normal course issuer bids during 2001, the Company acquired 233,500 common shares at an average price of $0.45 per share. The excess cost of acquisition over stated value of $93,561 was charged to retained earnings. The Company did not acquire any shares during 2002, and the bid expired on November 12, 2002.

Weighted average number of common shares

Earnings per share and cash flow from operations per share have been calculated based on the weighted average number of common shares outstanding during the year of 10,015,405 (2001 - 8,252,102).

9. Share capital *(continued)*

As the exercise price of all stock options was greater than the weighted average market price of the Company's shares in 2002, all options are anti-dilutive and therefore have been excluded from the diluted earnings per share calculation in 2002. As the exercise price of all stock options was less than the weighted average market price of the Company's shares in 2001, all options were dilutive and therefore have been included in the diluted earnings per share calculation. The diluted weighted average number of common shares outstanding during the year is 10,015,405 (2001 – 8,403,793).

Pro forma disclosure

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions used for grants in 2002: zero dividend yield; expected volatility of 132%; risk-free rate of 2.9%; and expected life of five years. The weighted average fair value of stock options granted during the year was $0.19 per option.

In management's opinion, had the Company accounted for employee stock options granted after January 1, 2002 using the fair value based method, the adjustment to the Company's pro forma net earnings and earnings per share would be insignificant.

10. Preferred shares

Because the redemption of the preferred shares was at the option of the holder, the redemption amount of the preferred shares was recorded as a non-current liability with a corresponding charge to retained earnings in 2000. As a result of the reverse takeover transaction (Note 2), the redemption feature of these preferred shares was terminated and accordingly their redemption amount has been added to retained earnings.

11. Lease commitments

The Company has operating leases on its office building, vehicles, and some office equipment. The future minimum annual payments under the lease are as follows:

2003	112,810
2004	13,295
2005	8,317
2006	579

12. Financial instruments

Fair values

The Company's financial instruments consist of cash, accounts receivable, bank indebtedness, bank loan, accounts payable and accrued liabilities, and long term debt. Unless otherwise noted, it is management's opinion that the Company is not exposed to significant interest, currency or credit risks arising from these financial instruments. The fair value of these financial instruments approximate their carrying values, unless otherwise noted.

Interest rate risk

The Company is exposed to interest price risk to the extent that the finance contracts bear fixed rates of interest.

Credit risk

The Company is exposed to credit risk on the accounts receivable from its customers. In order to reduce its risk, the Company requires bank letters of credit on all foreign sales. As such, the Company does not have significant exposure to any individual customer.

13. Changes in non-cash working capital

	2002 **$**	2001 $
Accounts receivable	**256,549**	(330,167)
Inventories	**26,659**	235,335
Prepaid expenses and other	**(15,316)**	(4,099)
Bank loan	**(60,000)**	(60,000)
Accounts payable and accrued liabilities	**(102,767)**	(318,248)
Deferred revenue	**(140,166)**	140,166
	(35,041)	(337,013)

14. Segmented information

The Company operates in two geographic segments within one industry segment. Product sales and services are provided to both Canada and Russia. The amounts related to each segment are as follows:

	2002		
	Canada $	Russia $	Total $
Revenue	824,936	443,705	1,268,641
Capital assets	521,556	-	521,556

	2001		
	Canada $	Russia $	Total $
Revenue	744,847	9,142,690	9,887,537
Capital assets	346,738	-	346,738

Corporate Information

Directors

I. Richard Ball [1]
Chairman of the Board of Directors
President and Chief Executive Officer,
Baden Technologies Inc.

Ian R. Ball
Director
Chief Financial Officer,
Baden Technologies Inc.

Robert Bolton [2]
Director

Dennis L. Nerland [1,2]
Director
Partner,
Shea Nerland Calnan

Gerald Olson [1,2]
Director

[1] Member Audit Committee
[2] Member Compensation Committee

Corporate Counsel
Joe Brennan
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